

Generally, a government contractor who purchases items to fulfill his obligations under a contract with a governmental unit purchases those items for use. See, U.S. v. New Mexico, 455 U.S. 720, 102 S. Ct. 1373 (1982). However, if the contract with the governmental unit explicitly requires the contractor to sell those items to the governmental unit, the purchase of those items by the contractor can be structured as purchases for the purpose of resale to the governmental unit. See 86 Ill. Adm. Code 130.2076. (This is a GIL).

March 28, 2002

Dear Xxxxx:

This letter is in response to your letter dated November 27, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at [www.revenue.state.il.us/Laws/regs/part1200/](http://www.revenue.state.il.us/Laws/regs/part1200/).

In your letter, you have stated and made inquiry as follows:

COMPANY, respectfully requests the Illinois Department of Revenue ('Department') issue a Private Letter Ruling pursuant to 2 Ill. Adm. Code Section 1200.110 with respect to the following factual situation.

**General Information:**

1. This Private Letter Ruling (PLR) is not requested with regard to hypothetical or alternative proposed transactions. The PLR is requested to determine the Retailers Occupation Tax consequences of actual business practices of COMPANY.
2. COMPANY is not currently engaged in litigation with the Department of Revenue in regard to this or any other tax matter.
3. COMPANY is not currently under audit by the Department in regard to any tax matter.
4. To the best of our knowledge, COMPANY has not previously requested the Department to rule on these specific matters for the company. In addition, the company has not submitted a similar issue to the Department.

5. COMPANY requests that certain information be deleted from the PLR prior to dissemination to others. The company requests that its name, address, location of its facility operations, and the name of representative be deleted.
6. COMPANY knows of no authority contrary to the authorities referred to and cited below.

### **Statement of Material Fact**

1. COMPANY is engaged in the contract operation and maintenance of water and wastewater treatment facilities and the disposal of water treatment residuals owned by twenty-one (21) different Illinois municipalities. The communities with current operation and maintenance contracts include:

#### **ILLINOIS LOCATIONS**

2. COMPANY provides these communities specialized operation, maintenance, and management services regarding their municipal water, wastewater, or public works facilities. In addition, COMPANY often provides the municipalities with the capability of single-source design-build-operate services and turn-key residuals management.

3. COMPANY services have proven to offer a number of advantages to Illinois municipalities:

- reduced costs via a variety of creative problem-solving initiatives;
- stabilized and better trained workforce;
- guaranteed costs for more predictable operating budgets;
- broad-spectrum experience; and
- reduced environmental liability.

4. As part of its contracts with Illinois municipalities, COMPANY has responsibility for the purchase, on behalf of the municipalities, of tangible personal property, materials, and supplies that are used to maintain, service, operate, and expand the municipally-owned facilities.

5. In reviewing COMPANY's typical expenditures, we found we have been paying sales tax on all items purchased on behalf of the municipalities. These purchases are tangible personal property that are ultimately attached to real estate owned by the municipality or consumed in maintenance or operation of the water or wastewater treatment plant operations.

The following items represent the significant purchases that are made throughout each year to operate and maintain the municipally-owned facilities:

- a. Electrical monitoring systems and equipment including above-ground and below-ground conduit and cabling.
- b. Underground and above ground piping for conveyance of water or wastewater water supply, natural gas supply, sewer supply, and other requisite systems.

- c. Manhole structures, lift stations, pumps, and wells facilities to transfer water and wastewater resources.
  - d. Chemicals to treat water and wastewater systems.
  - e. Electricity, natural gas, fuel to operate the systems of pumps and treatment systems.
  - f. Aeration basins and appurtenances.
  - g. Clarifiers.
6. To further complicate matters, the CITIES wastewater treatment plants are located in designated enterprise zones and 'qualified' purchases should satisfy requirements for an Enterprise Zone sales tax exemption.

### **Ruling Requested**

1. Each of the governmental bodies with an COMPANY contract has an active exemption identification number ('E' number) from the Department. As a contract operator for municipally-owned utility systems, qualified purchases made by COMPANY on behalf of the municipalities should qualify for a pass-through exemption for purposes of the Retailers Occupation Tax. (86 Ill. Adm. Code 130.2007 and 86 Ill. Adm. Code 130.2080).
2. In addition, many of the major materials identified and described above should also qualify for sales tax exemption as pollution control facilities for the purpose of the Retailer's Occupation Tax exemption. (86 Ill. Adm. Code 120.335).
3. Lastly, 'qualified' building material purchases for municipal facilities located in an enterprise zone should also qualify for exemption from sales tax if building material purchases are made in compliance with stipulations of the Enterprise Zone Act.

Relevant Authorities:

#### **1. Exemption under the Retailers Occupation Tax:**

In Illinois, organizations that are determined by the Department to be exclusively charitable, religious, educational, or a governmental body, are issued tax exemption identification numbers ('E' numbers)(86 Ill. Adm. Code 130.2007). Organizations holding such numbers are exempted from paying sales tax on organizational purchases that further their organizational purposes. Contractors who physically incorporate tangible personal property into real estate owned by holders of 'E' numbers can purchase such property tax-free by providing their suppliers with the certification described in Section 130.2075(d), as well as the 'E' number of the group into whose real estate that property will be incorporated. It is noted that only sales of tangible personal property invoiced to the organization or governmental body itself are exempt.

COMPANY provides contractual operation and maintenance of municipally-owned water, wastewater, and public works facilities.

**Conclusion 1:**

We respectfully request that the Department issue a ruling stating that for tangible personal property purchases invoiced and made on behalf of municipalities with 'E' numbers be considered exempt from sales tax regarding the ongoing operation and maintenance of municipally-owned water and wastewater facilities.

## **2. Exemption under the Pollution Control Facilities Law:**

Notwithstanding the fact that the sales may be at retail, sales of pollution control facilities are exempt from the Retailers' Occupation Tax. This exemption extends to and includes the purchase of pollution control facilities by a contractor who retransfers the facilities to his customer in fulfillment of a contract to furnish such pollution control facilities to, and to install them for, his customer. The phrase 'pollution control facilities' means any system, method, construction, device or appliance appurtenant thereto sold or used or intended for the primary purpose of eliminating, preventing, or reducing air and water pollution as the term 'pollution' is defined in the Environmental Protection Act [415 ILCS 5], or for the primary purpose of treating, pretreating, modifying or disposing of any potential solid, liquid or gaseous pollutant which if released without such treatment, pretreatment, modification or disposal might be harmful, detrimental or offensive to human, plant or animal life, or to property. This exemption includes not only the pollution control equipment itself, but also replacement parts therefore, but does not extend to fuel used in operating any such equipment nor to any other tangible personal property which may be used in some way in connection with such equipment, but which is not an integral part of the equipment itself. In addition, this exemption includes any chemical that is primarily utilized for filtration purposes as an integral component of a system for eliminating, reducing, or preventing pollution. Examples of the use of such chemicals include the use of chlorine, sodium hypochlorite, sodium hydroxide, hydrochloric acid, and nitric acid to filter pollutants in holding tanks.

### **Conclusion 2:**

We respectfully request the Department issue a ruling stating that COMPANY's purchase of pollution control materials made on behalf of municipalities are exempt from sales tax for qualified purchases under the Pollution Control Facilities Law.

## **3. Exemption under the Enterprise Zone Act:**

The Illinois Retailers' Occupation Tax Act [35 ILCS 120/2] imposes a tax on persons engaged in the business of making retail sales of tangible personal property. In accordance with Section 2-10 of the Act, this tax is measured by a seller's gross receipts [35 ILCS 120/2-10]. Pursuant to Section 5k of the Act [35 ILCS 120/5k], a retailer whose place of business is located within a county or municipality which has established an enterprise zone and makes sales of 'building materials' to be incorporated into real estate within the enterprise zone by remodeling, rehabilitation or new construction, may deduct receipts from such sales in the calculation of taxable gross receipts.

In order to qualify for the exemption provided in 35 ILCS 120/5k, certain procedural and documentation requirements must be satisfied. The retailer must be located in the municipality or unincorporated area of the county that established the enterprise zone into which the building materials will be incorporated. 86 Ill. Admin. Code Section

130.1951(a)(2) provides that this requirement will be satisfied if, at the time of the sale, the retailer:

- 1) has an identifiable presence in a municipality or county that has established an enterprise zone.
- 2) is registered as a retailer at a location in the municipality of unincorporated area of the county that has an established enterprise zone.
- 3) is able to document the acceptance of purchase orders at the registered location in the municipality or the unincorporated area of a county that established an enterprise zone.

86 Ill. Admin. Code Sec. 1951 further provides that two separate transactions must exist independent of each other and must be properly documented. The transactions are:

- 1) a sale from the supplier to the retailer who is located in the jurisdiction that created an enterprise zone; and
- 2) a sale from the retailer who is located in the jurisdiction that created an enterprise zone to the purchaser.

The following documentation establishes a sale from a supplier to a retailer who is located in the jurisdiction that created the enterprise zone:

- 1) a purchase order issued by the retailer to the supplier;
- 2) a Certificate of Resale issued by the retailer to the supplier;
- 3) an invoice from the supplier to the retailer; and
- 4) evidence of payment to the supplier from the retailer.

The following documentation establishes a sale from the retailer who is located in a jurisdiction that created an enterprise zone to a purchaser:

- 1) a purchase order issued by the purchaser to the supplier;
- 2) an exemption certificate issued by the purchaser to the retailer certifying that the materials will be incorporated into realty within the enterprise zone;
- 3) an invoice from the retailer to the purchaser; and
- 4) evidence of payment to the retailer from the purchaser.

To meet the above requirements, the COMPANY will establish retail business unit as an 'enterprise zone retailer'. They have physical presence in enterprise zone locations and will receive, accept and approve purchase orders at those locations. COMPANY will purchase 'building materials' to be incorporated into the municipally-owned realty within the enterprise zone. COMPANY will resell the building materials to itself as purchaser. COMPANY will then install and erect the building materials into the realty. Therefore, should be allowed to make tax-free sales of qualifying building materials to be incorporated into municipal realty within the Enterprise Zone.

In order to qualify for the deduction as provided in 35 ILCS 120/5k, the materials will constitute 'building materials' as provided in 86 Ill. Adm. Code Sec. 130.1951(a)(7). 86 Ill. Admin. Code Sec. 130.1951 (a)(7). That is, they must be purchased for *physical incorporation* into real estate. (Emphasis added)

The Department, in Private Letter Ruling 99-0009 (March 9, 1999), ruled that pipe racks, pipe, supports, and piping tie-ins installed at a natural gas fired power plant would constitute 'building materials' under the Department's regulations because they were permanently affixed to real estate. Further, since the real estate was located within an enterprise zone such items incorporated into real estate could be purchased tax-free from qualified retailers.

In a more recent decision, the Department in Private Letter Ruling ST 00-0013 (July 7, 2000) found that certain materials incorporated into realty within an electricity generating facility qualified as a building material pursuant to the Department's regulations. The Department found that turbine generators, electrical transformers, electrical cabling, piping and other materials that are permanently affixed to real estate qualify as a 'building material' for purposes of the deduction provided in 35 ILCS 120/5k and 86 Ill. Admin. Code Sec. 1951 (a)(1). Many of this letter ruling's facts and issues are similar to the COMPANY issues at hand in our request. Many of the materials at issue will be permanently and physically attached to the realty.

5 ILCS 120/k provides that a retailer whose place of business is located within a county or municipality which has established an enterprise zone, and who makes sales of 'building materials' to be incorporated into real estate in that enterprise zone by remodeling, rehabilitation or new construction, may deduct receipts from such sales in the calculation of taxable gross receipts. The deduction provided in 35 ILCS 120/5k is applicable to receipts from the sales of 'building materials.' In order to qualify as 'building materials,' the items must be physically incorporated into real estate. The materials in question qualify as 'building materials' for purposes of the deduction provided in 35 ILCS 120/5k.

### **Conclusion 3:**

COMPANY's purchase of 'qualified building materials' for use in enterprise zone locations qualify for sales tax exemption under the Enterprise Zone Act.

### **Final Conclusion**

We respectfully request the Department issue a letter ruling clarifying that qualified tangible personal property and material purchases made by COMPANY on behalf of municipalities are exempt from sales tax if the purchases are made in accordance with appropriate procedural methods for exemption depending upon which category the purchases fall within, as stated above.

Your clarification of the applicability of sales tax as it relates to the abovementioned purchases and circumstances is greatly appreciated.

If you have any questions or comments, please do not hesitate to contact me.

We are unable to grant you the private letter ruling you request. In order to grant a private letter ruling, we would need a separate letter ruling request for each local municipality, including a copy of your contract with them. Without reviewing your specific contractual obligations, we are

unable to rule on the issues you have described. We have tried unsuccessfully to contact you to discuss the need for this information. We hope the following general information is helpful.

In your letter, you indicate that you have contracts with local municipalities to operate and maintain their water and wastewater treatment facilities and to dispose of their water treatment residuals. You mention that as part of your contract, you purchase items on behalf of the municipalities that will be necessary to maintain, service, operate and expand the facilities. A recently adopted regulation discusses sales to purchasers performing contracts with governmental bodies. 86 Ill. Adm. Code 130.2076. Generally, a government contractor who purchases items to fulfill his obligations under a contract with a governmental unit purchases those items for use. See, U.S. v. New Mexico, 455 U.S. 720, 102 S.Ct. 1373 (1982). However, if the contract with the governmental unit explicitly requires the contractor to sell those items to the governmental unit, the purchase of those items by the contractor can be structured as purchases for the purpose of resale to the governmental unit. Our letter assumes that the municipality is considered an exempt entity by the Department for purposes of the sales tax laws. If your contract requires that you act as an agent of the municipality to purchase items on its behalf, you could use the municipality's exemption number (E number) to purchase the items tax-free. It would be necessary for us to examine the specific terms of your contract with the municipality to determine if this were the case, however.

If you sell the items to the municipality, then Section 130.2076 controls. The regulation states that "sales of tangible personal property to the contractor in this situation are exempt from Retailers' Occupation Tax as sales for resale if the following conditions are met:

- 1) There is a contract between the purchaser and the governmental body that requires the purchaser to provide tangible personal property to the governmental body.
- 2) The contract is specific in documenting a sale of tangible personal property from the purchaser to the governmental body. The contract must specify that the tangible personal property is transferred to the governmental body. However, the contract does not have to be item specific. For example, a statement that title to all of the tangible personal property that is purchased shall pass to the governmental body is sufficient. The transfer may be immediate or subsequent to the completion of the contract.

The exemption applies to all tangible personal property that is used or consumed in the performance of a contract with a governmental body and to which title passes to the governmental body under the terms of the contract.

You state in your letter that as a part of your contracts with the municipalities that you have responsibility for the purchase, on behalf of the municipalities, of tangible personal property, materials and supplies that are used to maintain, service, operate, and expand the municipally-owned facilities. In the case where you are making sales to a governmental body, you would give the supplier of these materials a certificate of resale. Your sales to the governmental unit under the contract provisions would then be exempt sales to a governmental body. However, as stated above, we need to examine your contracts to determine if you are purchasing on the municipalities' behalf or if you are selling to them.

For your information, we have enclosed a copy of 86 Ill. Adm. Code 130.335 concerning Pollution Control Facilities. The pollution control facilities exemption extends to "any system, method, construction, device or appliance appurtenant thereto sold or used or intended for the primary purpose of eliminating, preventing, or reducing air and water pollution as the term "pollution" is

defined in the Environmental Protection Act (415 ILCS 5/1 et seq.), or for the primary purpose of treating, pretreating, modifying or disposing of any potential solid, liquid or gaseous pollutant which if released without such treatment, pretreatment, modification or disposal might be harmful, detrimental or offensive to human, plant or animal life, or to property."

No items qualify for the Pollution Control Facilities exemption in and of themselves. No transactions are exempt on the basis of the pollution control exemption unless certifications are obtained as described in 86 Ill. Adm. Code 130.335(a) of the Department's rules. Items that can be used in both qualifying and non-qualifying activities must be used in qualifying activities before the exemption has application. We cannot determine if items qualify without a detailed description of each and its function.

Enclosed is a copy of 86 Ill. Adm. Code 130.1951 concerning Enterprise Zones. This regulation has been revised recently to reflect a recent change in the law and will be adopted shortly. Effective January 1, 2002, the deduction for the sale of building materials that will be incorporated into real estate in an enterprise zone has changed. Retailers who make a sale of building materials to be incorporated into real estate in any enterprise zone established by a county or municipality under the Illinois Enterprise Zone Act may deduct receipts from these sales when filing Form ST-1, Sales and Use Tax Return. Formerly, the retailer had to be located in the same jurisdiction that created the enterprise zone where the building materials would be incorporated into real estate.

However the new law provides that the jurisdiction in which the retailer is located can restrict the availability of the exemption through its enterprise zone ordinance. For example, if a contractor purchases building materials for incorporation into an enterprise zone in "City A" from a retailer in "City B," the availability of the exemption is governed by the "City B" enterprise zone ordinance. If the "City B" ordinance requires a "City B" building permit in order for the exemption to apply, the purchase of the building materials to be incorporated into "City A" will not qualify for the exemption. However, if a retailer is located in a jurisdiction that does not have an enterprise zone, there are no restrictions on the retailer concerning these sales. For example, if the contractor above purchases building materials from a retailer located in a municipality that has no enterprise zone ordinance, there are no restrictions on claiming the exemption. The purchase may be made tax-free. See Section 130.1951

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please visit our website at [www.revenue.state.il.us](http://www.revenue.state.il.us) or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

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Enc.